



The ETF Authority for Monday, June 2nd, 2003

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Published weekly on Sunday evening, [The ETF Authority](#) is a short-term swing trading newsletter that can help you profit from some of the most heavily-traded securities on the market -- exchange-traded funds (ETFs).

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(1.) MARKET SUMMARY

The stock market turned in yet another stellar week, with the S&P 500 rising more than 3% while the Nasdaq jumped around 6%. Even with those gains, the debt markets held their own, with only the long end of the bond market losing ground. The only equity-linked fund to fall was the Japan WEBS (EWJ), as the dollar rose, erasing the gains garnered by Japanese stocks in yen terms.

THE WEEK IN REVIEW

Surprising strength in the Chicago PMI and University of Michigan Consumer Confidence, with a little help from a drop in the terror alert level, helped U.S. equities jump to briefly move past last summer's high near 965. The S&P closed just a touch below that level on Friday, May 30th.

Overall though, economic data remains weak. I would only stand up and take notice if the national ISM Manufacturing Index also comes in much stronger than expected and if we start to see some strength in the jobs data, which is due out on Friday. Many market pundits suggest that payrolls are a lagging indicator. However, with just-in-time delivery and improved productivity models, any pick-up in demand should see a marked improvement in the labor data very quickly. Yet so far we have seen no such evidence of that.

ECONOMIC ANALYSIS

The stock market continues to ignore recent economic data. What does that mean? If this was the start of a new trend, then I would be quite concerned regarding my medium-term to long-term bearish leaning, for it would mean that there was something new playing on the market's psyche. Instead, I

believe we have a behavior that is growing long in the tooth here. (More on this topic in "Where do we go from here?" below.)

Last week's economic numbers were mixed. Although the consumer confidence data came in strong, and housing remains on fire as interest rates keep falling, durable goods orders fell twice as much as market consensus called for. Meanwhile, the second guesstimate on GDP was revised higher due to revisions in consumer purchasing data. However, consumer spending actually declined in April. This is not a good thing! There was one pleasant surprise: the Chicago Purchasing Managers index came in above 52, compared with expectations of sub-50 levels. However, employment fell again, as did the prices paid component.

The surprise from Chicago's report will likely push market consensus for the national ISM figure up closer to 50. Current consensus is for somewhere in the neighborhood of 47. Construction spending is expected to slip, though I do not see how given the housing numbers.

The big event next week will be non-farm payrolls. Consensus is for -25,000 after last month's loss of 48,000 jobs. This is one of those rare cases where I suspect consensus may be correct. However, an expected increase in the unemployment rate should weigh on the market. Continued soft earnings and hours worked numbers may prove to be the nail in the coffin.

WHERE DO WE GO FROM HERE?

One sentiment survey that I look at has now recorded its second consecutive week with more than 60% bulls. We last saw that back in August 2002, which turned out to be a major market top (it actually recorded three straight such readings at that time). There is still no signal of a top, but a major correction, and possibly reversal, is now brewing.

As I alluded to above, the market is consistently ignoring bad economic data and is jumping all over the good news. However, we've been doing this since the start of the hostilities in Iraq. Although consumer confidence has jumped strongly since then, purchases have not shown any follow through. The only other positive economic number I've seen since then was the Chicago PMI. That's not enough.

True, there is something to be said for all the money floating around the system from refinancings, but that is probably old news already. Most folks that are going to refinance have done so already. The \$400 per kid check many families will receive is not going to turn the economy around, although it won't hurt. Still, that won't hit until July/August anyway.

The bottom line is that unless the economy gets untracked, the stock market will fall. There is no sell signal as yet. I've noted before that my analysis points to an important market turnaround in late June, but I think we could see at least a minor correction from today's levels. That said, look for a range of 880 to even levels a bit above 1,000 on the S&P over the next few weeks before we come crashing down beginning in late June.

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(2.) WEEKLY ETF PERFORMANCE

Below you'll find a table of weekly performance data for all ETFs that I track for this newsletter...

<u>Name (Ticker Symbol)</u>	<u>Open</u>	<u>High</u>	<u>Low</u>	<u>Last</u>	<u>Change</u>	<u>% Change</u>
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Major Indices

Dow Diamonds (DIA)	85.72	88.98	85.60	88.84	2.61	3.0%
S&P 500 SPDR (SPY)	93.30	97.09	93.18	96.95	3.19	3.4%
Nasdaq-100 Index (QQQ)	27.93	29.87	27.90	29.79	1.69	6.0%
Russell 2000 iShares (IWM)	83.27	88.15	83.27	88.03	4.63	5.6%
S&P 400 Mid-Cap (MDY)	83.06	87.14	83.05	87.13	3.74	4.5%

International Indices

Japan Webs (EWJ)	6.73	6.84	6.68	6.79	-0.01	-0.1%
Canada Webs (EWC)	11.22	11.50	11.21	11.50	0.21	1.9%

Fixed Income Indices

1-3 Year Lehman U.S. Govt. Bond iShares (SHY)	82.66	82.73	82.59	82.68	0.02	0.0%
7-10 Year Lehman U.S. Govt. Bond iShares (IEF)	89.26	89.39	88.47	89.31	0.11	0.1%
20+ Year Lehman U.S. Govt. Bond iShares (TLT)	95.62	95.71	93.31	94.60	-1.25	-1.3%
iShares GS \$ InvesTopTM Corporate Bond Fund	115.63	115.73	114.30	115.55	0.02	0.0%

Other Equity Index Based ETFs

Russell 1000 Value (IWD)	48.72	50.50	48.55	50.37	1.47	3.0%
Russell 2000 Growth (IWO)	44.38	47.19	44.15	47.19	2.79	6.3%

Sector-based ETFs

Biotech HOLDR (BBH)	114.85	120.70	114.85	120.25	5.05	4.4%
Nasdaq Biotech iShares (IBB)	64.90	68.30	64.70	68.06	4.37	6.9%
Energy SPDR (XLE)	24.04	24.64	24.00	24.48	0.36	1.5%
Financial SPDR (XLF)	23.35	24.60	23.35	24.56	0.95	4.0%
Oil Service HOLDR (OIH)	63.25	64.82	62.21	64.22	0.74	1.2%
Pharmaceutical HOLDR (PPH)	75.14	77.25	74.80	76.63	0.95	1.3%
Retail HOLDR (RTH)	75.50	79.32	75.28	78.90	3.05	4.0%
Semiconductor HOLDR (SMH)	26.92	30.20	26.91	29.95	2.83	10.4%
Software HOLDR (SWH)	29.75	31.70	29.73	31.51	1.66	5.6%
Technology SPDR (XLK)	16.00	17.03	16.00	16.95	0.81	5.0%

(3.) ETF RELATIVE STRENGTH MONITOR

(Note: If you're a first-time reader or you are otherwise unfamiliar with our proprietary **ETF Relative Strength Monitor**, then please [click here](#) for a brief description.)

The technology sector moved sharply up our rankings last week, as the Semiconductor HOLDR (SMH, \$29.95), which brought up the rear a week ago, was the top performer in the week past. That did not help our model portfolio, which though ahead on a two-week basis, underperformed the broad market last week (see below for more). Happily, the number one stock in our ranking scheme, and the second-best performer for the week, was the Nasdaq Biotech iShares (IBB, \$68.06), which we also hold.

The bond market, despite its recent strength, remains near the bottom of our list, as the recent jump in stocks has left the debt market in the dust. Along with the Pharmaceutical HOLDERS (PPH, \$76.63) and the Japan WEBS (EWH, \$6.79), all four of the debt-related ETFs we track finished in the bottom six positions of our **Relative Strength Monitor**.

Upcoming opportunities will probably present themselves via shorts in the Technology and Biotech sector and purchases in the bond market, but won't make for good trades until equities turn tail. Until then, the risk is that the bond market could ease some and stocks could continue a bit higher. I suspect we might see a blow-off top in the very short term.

Here is this week's **ETF Relative Strength Monitor**...

<u>Name (Ticker Symbol)</u>	<u>1-week return</u>	<u>4-week return</u>	<u>13-week return</u>	<u>ETF Relative Strength Rank</u>	<u>Change from Last Week</u>	<u>4-week Average Rank</u>
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Major Indices

Dow Diamonds (DIA)	3.03%	3.53%	12.16%	7	-2	5.5
S&P 500 SPDR (SPY)	3.40%	4.01%	14.65%	8	-2	9
Nasdaq-100 Index (QQQ)	6.01%	5.34%	18.40%	18	10	12.75
Russell 2000 iShares (IWM)	5.55%	8.28%	22.52%	19	2	16.5
S&P 400 Mid-Cap (MDY)	4.48%	6.71%	17.13%	16	0	13.5

International Indices

Japan Webs (EWJ)	-0.15%	3.35%	-0.73%	1	-13	8.75
Canada Webs (EWC)	1.86%	8.18%	15.00%	13	-7	17.5

Fixed Income Indices

1-3 Year Lehman U.S. Govt. Bond iShares (SHY)	0.02%	0.47%	0.41%	2	0	1.5
7-10 Year Lehman U.S. Govt. Bond iShares (IEF)	0.12%	4.27%	2.83%	5	-6	7.5
20+ Year Lehman U.S. Govt. Bond iShares (TLT)	-1.30%	7.11%	4.96%	6	-12	14
iShares GS \$ InvesTopTM Corporate Bond Fund (LQD)	0.02%	3.68%	4.98%	3	-9	7

Other Equity Index Based ETFs

Russell 1000 Value (IWD)	3.01%	4.98%	15.74%	8	-5	10.5
Russell 2000 Growth (IWO)	6.28%	9.06%	16.06%	21	6	17

Sector-based ETFs

Biotech HOLDR (BBH)	4.38%	15.07%	35.26%	20	-2	17
Nasdaq Biotech iShares (IBB)	6.86%	14.48%	42.24%	23	1	19.75
Energy SPDR (XLE)	1.49%	8.37%	9.83%	11	-8	13
Financial SPDR (XLF)	4.02%	3.50%	17.18%	12	9	8
Oil Service HOLDR (OIH)	1.17%	14.92%	11.28%	13	-8	18.75
Pharmaceutical HOLDR (PPH)	1.26%	-2.03%	8.46%	4	3	5.75
Retail HOLDR (RTH)	4.02%	2.08%	18.86%	10	5	8.5
Semiconductor HOLDR (SMH)	10.44%	9.91%	27.23%	22	15	14.25
Software HOLDR (SWH)	5.56%	5.00%	16.75%	17	11	13
Technology SPDR (XLK)	5.02%	5.34%	16.74%	15	11	14

(4.) MODEL ETF PORTFOLIO

	<i>S&P 500</i>	<i>Model Portfolio</i>
Last Week	+3.25%	+1.57%
Since Inception	+2.04%	+2.77%

Here are instructions for this week (barring any revisions we may make in the middle of the week via a special News Flash):

- We remain short SMH. Place a buy stop for 200 shares at \$30.21. If this trade gets triggered, then as a net result (remember, we are currently short 100 shares) we will then be long 100 shares of SMH. If the buy stop at \$30.21 is hit, then immediately place a stop loss on this trade at \$29.59.
- Put a sell stop on IBB at \$65.92. I may issue further guidance on this position via a special News Flash later in the week.
- Put a sell stop on XLE at \$24.00. I may issue further guidance on this position via an intraweek News Flash.
- I will advise replacements during the week if these trades are executed.

Our returns trailed the market last week due to our call sale (which I expect will help our returns in the end, as stocks should turn lower before the options expire), and the short on SMH. I wanted to find a dip to buy it back, and we did not get it. We might be in a blow-off position here, but it is worth waiting to see if that occurs, since when the market turns, both SMH and our current long, IBB, will likely get hit hard. (IBB could be due for a round of profit taking largely because it is ahead by more than +40% in the past 13 weeks!)

MODEL ETF PORTFOLIO

<u>ETF Name</u>	<u>Sym</u>	<u>Position</u>	<u>Entered</u>	<u>Entry Price</u>	<u>Begin Value</u>	<u>Current Price</u>	<u>Current Value</u>	<u>Div</u>	<u>Chg</u>	<u>%Chg</u>
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Dow Diamonds	DIA	100	19-May	\$86.99	\$8,699	\$88.84	\$8,884	\$0	\$185	2.13%
Nasdaq Biotech iShares	IBB	100	19-May	\$61.76	\$6,176	\$68.06	\$6,806	\$0	\$630	10.20%
Energy SPDR	XLE	99	19-May	\$23.59	\$2,335	\$24.48	\$2,424	\$0	\$88	3.77%
Semiconductor HOLDR	SMH	-100	19-May	\$27.81	-\$2,781	\$29.95	-\$2,995	\$0	-\$214	-7.70%
DIA June 88 call	DAVFJ	-1	26-May	\$0.65	-\$65	\$2.00	-\$200	\$0	-\$135	-208%
Cash					\$9		\$9			
<u>Portfolio Totals</u>			<u>19-May</u>		<u>\$20,000</u>		<u>\$20,554</u>	<u>\$0</u>	<u>\$554</u>	<u>2.77%</u>
S&P 500 Index	SPX		19-May	944.30	\$944	963.59	\$964	\$0	\$19	2.04%

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(5.) TRADE OF THE WEEK

I actually have two trades this week: One is a breakout trade, which I will closely trail higher, and the other is a short sale on a trendline break.

BUY 300 SHARES SOFTWARE HOLDR (SWH, \$31.51) ON A MOVE ABOVE \$31.79

The Software HOLDR moved into the upper quartile of our relative strength rankings last week with a +5.56% gain. However, this ETF has gained just +16.75% over the past 13 weeks, which puts it well behind several other ETFs and leaves the fund less overbought than many of the other ETFs we track for this newsletter. A move north of \$31.79 would put prices above their January 2003 peak. It would also likely result in a break of the RSI momentum divergence trendline. In addition, it would negate bearish candlestick patterns. With fairly tightly trailed stops, this becomes a low-risk trade.



I like this trade because:

- RSI down trendline is about to break.
- SWH is set to make a new high for 2003.
- Move above \$31.70 would negate bearish candlestick pattern.
- Less overbought than other ETFs, but still showing strength.

RECOMMENDATION:

BUY 300 SHARES SWH WITH A BUY STOP ORDER AT \$31.80, LIMIT \$31.90.

TARGET: \$35.49

STOP: Place your initial stop at \$30.87, but on a rally above \$32.00, trail this stop up to your purchase level.

Assuming a purchase at \$31.80 and sale at \$35.49, your profit would be \$1,107, or +11.6%.

SELL SHORT 100 SHARES OIL SERVICE HOLDR (OIH, \$64.22) ON A CLOSE BELOW ITS CURRENT UP TRENDLINE

Oil Service HOLDRs have been fairly volatile recently. They show potential to move slightly higher early in the week, but are in danger of sliding below steep trendline support in the coming days. With momentum divergences, an approaching bearish crossover in MACD, and oil prices set to decline again, OIH is at risk of a substantial decline. This ETF also shows up as a middling sector in our rankings and was only able to gain +1.26% last week.



I like this trade because:

- RSI momentum divergence.
- Trendline break coming.
- Oil prices look set to correct.
- MACD could have a bearish crossover.

RECOMMENDATION:

SELL SHORT 100 SHARES OIH ON A CLOSING TRENDLINE BREAK (sell the following morning as long as price is within \$0.15 of prior day's close in either direction). Closing sell levels will be \$63.11 on Monday, \$63.53 on Tuesday and \$63.94 on Wednesday.

THIS RECOMMENDATION EXPIRES IF THE TRADE IS NOT ENTERED BY THURSDAY MORNING.

TARGET: \$60.04, although I might revise this lower if the market starts to fall sharply.

STOP: \$64.83

Assuming a sale at \$63.11 and close at \$60.04, your profit would be \$307, or +4.9%.

(6.) CONTINUED GUIDANCE ON PREVIOUS TRADES

LONG SIX (6) NASDAQ 100 TRUST (QQQ, \$29.79) SEPTEMBER 2003 27 PUTS (QAVUA, \$0.90)

DATE RECOMMENDED: 05/19/2003

DATE ENTERED: 05/19/2003

BOUGHT SIX QAVUA AT \$1.40

STOPPED ON 05/27/2003: \$0.95

We were stopped out of this options position last Tuesday. *This trade is now closed.*

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SOLD SHORT 1,000 SHARES TECHNOLOGY SECTOR SPDR (XLK, \$16.95) AT \$16.26

DATE RECOMMENDED: 05/26/2003

DATE ENTERED: 05/27/2003

ENTRY PRICE: \$16.26

STOPPED ON 05/27/2003: \$16.54

We were stopped out of this short position last Tuesday. *This trade is now closed.*

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Thanks again for reading this week's issue, and good trading in the week ahead!



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